

# Negotiating the MOU from the Perspective of the Head of the Israeli Negotiating Team

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The latest memorandum of understanding (MOU) on US foreign defense aid to Israel was signed in September 2016 after over three years of negotiations. The negotiations went through ups and downs, and were even temporarily suspended at one point. The new agreement covers 10 years (2019-2028), during which total American aid will be increased to \$38 billion: \$33 billion in ordinary defense aid (foreign military financing – FMF), compared with \$30 billion in the previous agreement, and \$5 billion in a new multi-year agreement for ballistic missiles defense (BMD), compared with \$400 million annually with no multi-year commitment in the preceding decade.

The process began in March 2013 during US President Barack Obama's visit to Israel. The visit was designed mainly to soften the Israeli position on two issues: the agreement with Iran and relations with Turkey, following the *Marmara* incident. As is customary with visits by a US president to Israel, Obama realized that he had to give something in return for the compromise that was achieved on the Turkish issue, and for his wish for progress on the Iranian issue (although the messages that he received during the visit were clear: Israel is against a deal with Iran if it does not include a total closure of the nuclear program and all its derivatives). It appears that in the absence of alternatives for a possible gesture to Israel, Obama announced that he had

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instructed his staff to form a joint committee for the purpose of reaching a new agreement on aid to Israel – five years before the current agreement expired. This instruction surprised everyone, because the agreement was in effect until the end of 2018, and renewal negotiations usually begin only two years before the end of an existing agreement.

The talks between the parties began in the summer of 2013. At the time, I was head of the Division for Strategic Development and Organization and deputy head at the National Security Council (then headed by Major General [res.] Yaakov Amidror). The interministerial team formed to accompany me included representatives of all of the relevant agencies (Ministry of Defense – the Defense-Political Branch and the Budget Department, Ministry of Foreign Affairs, Ministry of Finance – Accountant General's Department and Budget Department, IDF – Planning Directorate and the Chief of Staff financial advisor, the Israeli embassy in Washington – Ambassador Ron Dermer and Defense Attaché to the United States Yaacob Ayish). The team worked with complete synergy and cooperation; even if there were initially disagreements on a number of issues, they were usually resolved without becoming publicly known. The American team was led by Special Assistant to the President and White House Coordinator for the Middle East, North Africa, and the Gulf Region on the US National Security Council, Philip Gordon, under US National Security Advisor Susan Rice.

Despite the tension between President Obama and Prime Minister Benjamin Netanyahu at the time, the two sides wanted to reach an agreement that would meet the needs of both countries and continue the special relationship and strategic alliance between them.

For about a year, a number of work meetings between the teams took place in Israel and Washington. During those meetings, the Israeli position was presented to the American team in four separate sections. The first section, for which the Defense-Political Branch in the Ministry of Defense was responsible, included an analysis of the general state of the Middle East and the potential threats to Israel in 2023. The second section, prepared by the Ministry of Defense budget department and the Ministry of Finance, was devoted to a macroeconomic analysis of the Israeli economy and the defense budget within the state budget. The third (and largest) section, for which the IDF, led by its Planning Directorate, was responsible, focused on the IDF's needs and force building. In this section, a detailed theoretical

model was constructed, excluding budgetary constraints, showing the needs of the defense establishment in shekels and foreign currency. In the fourth section, the National Security Council presented the process for continuing the negotiations and the desirable structure for the aid agreement, in light of the preceding sections.

The budget for assistance in ballistic missile defense was not included in the discussions at this stage. Most of the early talks concerned the dire state of the American economy, Israel's needs, and the amount of assistance that could be given to Israel as part of FMF. The basic American position was that aid had to be the same or less than in the existing agreement. In order to justify a requested increase in the amount of aid, the Israeli team presented economic analyses of the decline in the dollar's purchasing power and the rising cost of maintaining and owning the main battle systems, adjustments needed for inflation in Israel and the US, macroeconomic assessments of both countries, and the projected Israeli defense budget.

After about a year of discussions, we presented a draft agreement, but we had not yet reached the stage at which it was acceptable to our American colleagues. In the background, progress was being made in American contacts with Iran aimed at reaching the nuclear agreement, to which Prime Minister Netanyahu was strongly opposed. To President Obama's dismay, Netanyahu spoke to the US Congress in March 2015. In his speech, Netanyahu thanked the United States for its ongoing support for Israel, but did not conceal his determined opposition to the emerging agreement with Iran. The speech exacerbated the rift between the two leaders; as a result, the talks on the new aid agreement were suspended for an extended period.

Paradoxically, the talks were renewed after the nuclear agreement was signed with Iran in the summer of 2015. It is possible that Obama wanted to leave a positive impression in his relations with Israel, and it was also possible that considerations pertaining to the US presidential election campaign, which was just beginning, played a role. Obama may also have been responding to Hillary Clinton's effort to restart the negotiations on the aid agreement (Clinton had been Obama's secretary of state and now was running for the presidency). The Israeli policy dictated by the prime minister was to accept the American offer to renew the talks separately from the Iranian nuclear issue in order to highlight the depth of the strategic relations between the

countries (stronger than the dispute), and to enable the IDF to go ahead with its multi-year plan.

Obama appointed US National Security Council Senior Director for the Levant, Israel, and Egypt Yael Lempert to head the American team, which included senior officials from the Departments of Defense, State, and the Treasury, with very active involvement by US Ambassador to Israel Daniel Shapiro. The team was constantly guided by Susan Rice, who was involved in every detail in the negotiations. The Israeli team was composed of the same agencies that constituted the original team (with different people in some cases, as expected). When I was appointed as acting Israel National Security Council head in early 2016, Susan Rice asked me in our first meeting whether I was attending the meeting as head of the negotiating team or as head of National Security Council responsible for it. I smiled and answered that I was fulfilling both functions.

Behind the scenes and discretely, the team heads established a number of clear “game rules,” especially regarding two matters that all agreed would not be included in the discussions: the Iranian nuclear agreement (not as a factor that should increase the amount of aid because of a greater threat, and not as a factor that should reduce the aid because of a lesser threat) and the Palestinian question, which would not be raised under any circumstances as a condition for signing the aid agreement. At this stage, the Americans asked that aid for BMD be included in the negotiations.

When the talks were renewed, the Americans presented four basic demands, which we did not fully accept:

1. Complete termination of conversion of part of the aid (26.4 percent) to shekels for the purpose of off-shore procurement (OSP) of systems and equipment to the systems purchased in the United States with the aid money. The unequivocal position by Susan Rice presented to me in a face-to-face meeting was “*no conversion from the first year of the agreement.*”
2. A halt in the use of the aid budget to purchase fuel from American companies.
3. Preserving the balance between an increase in the amount of aid and the increase in the defense budget. The unequivocal position was that every nominal increase in the aid agreement would be accompanied by an increase in the defense budget. From the American perspective, it was unacceptable for Israel’s defense budget to be decreased (this was

reported at the time in the Israeli media) when the American aid budget was increased.

4. Most of the money in the agreement was to be earmarked in advance for procurement of specific American weapons systems (type and quantity), and no general agreement would be signed on the annual amount of aid; the precise content would be determined each year. The American team planned to demand that Israel state which systems would be procured with the aid money, according to the team's analysis of the threat in a given theater, and the Israeli response needed in order to preserve Israel's relative advantage.

In the second round of talks, the Israeli team returned to the same four (revised) professional sections established in the first round. We set for ourselves two main principles, according to which we constructed the presentation and the Israeli requirements:

1. The agreement will be in effect in 2019-2028, and therefore cannot be assessed from a perspective of the current situation and threat or only according to the forecast for the next few years. It cannot be a type of work plan. The point in time selected as a reference was 2023, the middle of the period. When an analysis of this reference point is agreed, no scenario can be removed from the agenda, including a conventional war scenario. The force-building process must therefore include readiness for a broad range of scenarios.
2. Israel's revised defense needs (in dollars and shekels) far exceed what the United States is capable of providing in the aid agreement and what Israel is capable of allocating to the defense budget in its government budget. The main conclusion from this principle was that the discussion could not center on the precise scope of needs, which systems the United States would transfer to Israel, and in what quantity, since it is clearly impossible to meet all of the needs, on the one hand, and on the other, it is impossible to predict in advance what needs will require the highest priority. The question, then, is not what and how much is needed, but how much the United States is able and willing to give to Israel.
3. The presentation of these principles, which were gathered from a detailed and reliable database, was a great success, and convinced the Americans that it was impossible to pre-determine in the aid package

which systems would be procured. Similarly, it is impossible to dictate to Israel in advance which systems it must procure with the aid budget. Following our detailed presentation, the Americans abandoned their own outline, which included their position on the scope of Israel's needs and a proposal for the systems that the agreement would include. They decided to work with our data, and to focus the discussion on the framework of the agreement and its indirect terms. It is my professional opinion that the comprehensive preparations we made in Israel and the high-quality meetings we held with the American team paved the way to the new agreement.

In mid-2016, we concluded the discussions and reached understandings that Israel would receive \$3.3 billion a year in American FMF. Two issues were still in dispute: purchase of fuel and conversion of aid to shekels for OSP. Regarding the fuel, at the time, the inclination was to attach a document side letter to the agreement stating that we would not purchase fuel with FMF without the other side's agreement. In the final stages of the negotiations, the Americans (including the president) insisted that this commitment be part of the agreement. After further deliberations, a clause was inserted into the agreement (similar to the general legal principles governing the use of FMF) stating that the United States and Israel had agreed that "FMF is not intended for fuels and consumables."

The thorniest issue concerned the agreement to convert part of the aid to shekels for use in Israel as support for the systems purchased with dollars in the United States. In the previous agreements, Israel received permission to convert 26.4 percent of the dollar aid into shekels for procurement in Israel. One of the arguments made by the Americans in their demand for ending this conversion option from the first day of the new agreement was that this option originally stemmed from the desire to help Israel establish a defense industry and put it on its feet. Today, the Israeli defense industry is thriving, and it is unacceptable for Israel to convert American dollar aid into shekels, invest it in the development of state-of-the-art products, and eventually compete with American companies over these products throughout the world. These inaccurate contentions, according to which Israel is using the shekel conversion budget for research and development, are of course incorrect. Unfortunately, however, they were disseminated and

reinforced by various parties, including Israelis, who were unfamiliar with the data – a fact that hindered us in the negotiations. According to the aid agreements with the United States, Israel is not allowed to use the shekels converted from dollar aid for R&D. Each year, Israel details to the American administration where the converted money is invested in order to prove that it is being invested solely in compliance with the rules. The claims by some industries and irresponsible senior administration officials that halting the aid conversion arrangement would harm Israeli R&D greatly hampered us during the negotiations, and we worked hard to rectify the situation. During the discussions on this issue, Susan Rice reiterated several times that if we did not accept the American position, no agreement would be reached, and if this is what we wanted, we could wait for the next administration.

Following the long and exhausting negotiations, in which then-IDF Planning Directorate head Major General Amikam Norkin and then-IDF Budget Division head Brigadier General Sasson Hadad took part and innumerable compromise formulas were proposed, we reached an agreement that did eliminate conversion of aid dollars into shekels, as Rice had demanded, not at the outset of the agreement, in 2019, but only in 2028, the last year. We were also in accord that the new agreement would include approximately 70 percent of the conversion amount approved in the old agreement, and that the reductions in conversion in the first five years would be purely symbolic. According to this compromise, the conversions were to be reduced gradually, not a dagger thrust starting in 2019, as the Americans initially wanted.

The compromises that we reached on this topic were very important, and will provide the defense industries in Israel, with an emphasis on the small companies, with an extended period to prepare for the change, with the help of government ministries and the large industries. It is important to keep in mind that the agreement was signed two years before the expiration of the preceding agreement, so that a total of seven to nine years was given to prepare for the change (unfortunately, not all of the parties have taken advantage of this time to prepare thus far, but it is not too late to start).

As part of the agreement, the Americans also sought to reach 10-year understandings about the amount of aid for joint BMD projects in order to avoid repeating these discussions every year (and probably also in order to present a bigger hike in aid to Israel by the Obama administration). The White House did not like the annual Congressional debates at which various



parties tried to obtain more support for the joint projects. A majority on the Israeli side also supported reaching decade-long understandings, which would enable better planning of joint projects and avoid the annual effort involved in submitting aid requests to Congress. We ultimately agreed on \$500 million a year for 10 years – a total of \$5 billion for joint projects. The language of the new agreement was copied exactly from the previous agreements in order to preserve all of the existing understandings.

In September 2016, we reached a final draft of the MOU for a sum of \$38 billion over a decade: \$33 billion in FMF and \$5 billion for BMD. Just before the time came to sign it, a last obstacle arose from the direction of US Senate Finance Committee Chairman Lindsey Graham, which itself was caused by the ongoing tension between the White House and Congress concerning responsibility for defense aid. Following a number of exchanges, including letters at the highest levels, this problem was also solved. After over three years of discussions, the MOU for defense aid to Israel in 2019-2028 was signed in November 2016.

It should be stressed that contrary to the rumors and leaks on the matter, at no stage in the negotiations between the teams was a better agreement offered to Israel in exchange for ceasing its opposition to the nuclear agreement. This matter was never raised. Furthermore, because of legal and fiscal constraints, the US administration had no practical way of offering substantially higher sums than those eventually agreed. All of the statements on the subject, mainly in Israel, by parties not directly involved in the negotiations were in my opinion due either to incorrect analysis of the data or unrelated motives. I believe that the agreement reached was very good for Israel, and was signed at the right time, for the following reasons:

1. The amount on which we agreed was higher than any amount that we received in the past.
2. Early on, many argued that we would be unable to obtain anything near what we received in the preceding agreement from President Obama and the United States, in the wake of the financial crisis. Furthermore, the US' total foreign aid budget is predetermined; any increase in aid to Israel would necessarily reduce the amount available for other countries.
3. Could we have obtained a better agreement with a new administration? I am one of those who believe that we did well to sign the agreement with



the Obama administration, despite the tensions and disagreements with it. Moreover, the signed MOU underscores the bipartisan support for Israel.

4. While the new agreement cuts the amount of aid that can be converted into shekels, the cut is gradual and very small in the early stages of the period covered therein. It allows for lengthy preparation (seven-nine years) for the new situation.
5. The new agreement increases total FMF for Israel by \$3 billion in comparison with the current situation. Offset (reciprocal) procurement alone will increase investment in the Israeli defense industry by approximately \$1 billion, which amounts to a large chunk of the reduction in aid conversion. Offset procurement is not binding on the US under the formal terms of the aid agreement, so it will go mainly to the large industries, but history proves that the Americans are committed to making their best effort in this matter, and more.

The signing of the agreement was a superb achievement that enabled Israel to preserve its strategic alliance and cooperation with the United States. It highlighted the overall long-term commitment of the United States to Israel. And it enabled the defense establishment to plan its budget and procure essential platforms for the very long term.